Market & Economic Review

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The following market update was provided by Vanguard Investment Strategy Group and is forwarded by Independent Wealth Management.

Vanguard Market Perspectives Key Takeaways

- Following the U.S. Federal Reserve's interest rate cut of 0.50%, we expect the Fed to cut its rate target by an additional 50 basis points this year, ending at 4.25%-4.50%.
- We foresee further rate cuts in the U.K. and Euro area, with core inflation projected to reach the BOE's and ECB's 2.00% targets in 2025.
- Due to the sluggish domestic demad, China's target of 5.00% economic growth by year-end is at risk. We believe this target will still be met provided that a suffuiciently timely policy response occurs.

3Q24 Benchmark Returns

	3Q	2024
Equities		
S&P 500 Total Return Index	5.9%	22.1%
Russell Index 1000 w/Dividend	6.1%	21.2%
Russell Index 2000 w/Dividend	9.3%	11.2%
Russell Index 3000 w/Dividend	6.2%	20.6%
MSCI Developed EAFE (USD)	7.3%	13.5%
MSCI Emerging Markets (USD)	7.8%	14.4%
Alternatives		
Credit Suisse Hedge Fund Index	-0.5%	6.3%
DJ Wilshire Global REIT Index	14.8%	9.0%
iShares S&P US Pref Stock Index	5.8%	7.0%
S&P GSSI Natural Resources Index	1.0%	10.7%
Barclays High Yield Bond Index	5.3%	8.0%
Fixed Income		
90 Day Treasury Bill	1.3%	3.9%
Barclays Muni Bond Index	2.7%	2.3%
Barclays Aggregate Bond Index	5.2%	4.4%
Barclays Global Bond Index	9.4%	2.0%

Independent Wealth Management

Jay Berger, CFP®
jay.berger@iwmusa.com

Steve Fisher, CFP®
steve.fisher@iwmusa.com

Scott Hackney, CFP®
scott.hackney@iwmusa.com

236 1/2 East Front Street
Traverse City, Michigan 49684
231 929 1086 tel
888 929 1086 toll free
231 346 5959 fax
www.iwmusa.com

Vanguard

Market perspectives

Vanguard's monthly economic and market update

The views below are those of the global economics and markets team of Vanguard Investment Strategy Group as of September 19, 2024.

KEY HIGHLIGHTS

- **Following the U.S. Federal Reserve's interest rate cut of 0.50%**, we expect the Fed to cut its rate target by an additional 50 basis points this year, ending at 4.25%–4.50%.
- We foresee further rate cuts in the U.K. and Euro area, with **core inflation projected to reach the BOE's and ECB's 2.00% targets in 2025**.
- Due to sluggish domestic demand, **China's target of 5.00% economic growth by year-end is at risk.** We believe this target will still be met provided that a sufficiently timely policy response occurs.

Vanguard's outlook for financial markets

Our 10-year annualized nominal return and volatility forecasts are shown below. They are based on the June 30, 2024, running of the Vanguard Capital Markets Model® (VCMM). Equity returns reflect a 2-point range around the 50th percentile of the distribution of probable outcomes. Fixed income returns reflect a 1-point range around the 50th percentile. More extreme returns are possible.

Equities	RETURN PROJECTION	MEDIAN VOLATILITY
U.S. equities	3.2%–5.2%	17.0%
U.S. value	4.7%–6.7%	19.3%
U.S. growth	0.1%–2.1%	18.1%
U.S. large-cap	3.0%–5.0%	16.7%
U.S. small-cap	5.0%–7.0%	22.6%
U.S. real estate investment trusts	4.2%–6.2%	19.9%
Global equities ex-U.S. (unhedged)	6.9%–8.9%	18.4%
Global ex-U.S. developed markets equities (unhedged)	7.0%–9.0%	16.8%
Emerging markets equities (unhedged)	5.7%–7.7%	26.1%
Fixed income		
U.S. aggregate bonds	4.5%–5.5%	5.7%
U.S. Treasury bonds	4.2%–5.2%	5.9%
U.S. intermediate credit bonds	4.8%–5.8%	5.2%
U.S. high-yield corporate bonds	5.6%–6.6%	10.0%
U.S. Treasury Inflation-Protected Securities	3.5%–4.5%	5.1%
U.S. cash	3.9%–4.9%	1.4%
Global bonds ex-U.S. (hedged)	4.4%–5.4%	4.4%
Emerging markets sovereign bonds	5.6%–6.6%	10.0%
U.S. inflation	1.9%–2.9%	2.3%

IMPORTANT: The projections or other information generated by the Vanguard Capital Markets Model® regarding the likelihood of various investment outcomes are hypothetical in nature, do not reflect actual investment results, and are not guarantees of future results. Distribution of return outcomes from the VCMM are derived from 10,000 simulations for each modeled asset class. Simulations are as of June 30, 2024. Results from the model may vary with each use and over time. For more information, see page 4.

Source: Vanguard Investment Strategy Group.

Notes: These probabilistic return assumptions depend on current market conditions and, as such, may change over time.

Region-by-region outlook

United States

The Federal Reserve cut its policy interest rate by 0.50 percentage points on September 18, to a range of 4.75%–5.00%, but did so in the context of economic resilience rather than concerns about a material slowdown. We expect:

- **The Fed** to cut its rate target by an additional 50 basis points this year, ending at 4.25%–4.50%. We foresee additional cuts in 2025 that would bring the policy rate toward the neutral rate, which we peg at a nominal 3.50%.
- **Economic growth** to cool but remain at a near-trend pace of 2.00% by year-end.
- The pace of **core inflation**, measured by the Fed's preferred gauge, personal consumption expenditures, to rise by year-end to 2.90% on a year-over-year basis, because of base effects, or challenging comparisons with year-earlier data.
- The **unemployment rate** ending the year marginally above current levels. It measured 4.20% in August.
- **Interest rates** to not return toward their pre-COVID near-zero levels, aligning with our view that we have returned to an era of sound money.

Euro area

On September 12, the central bank announced the second cut to its policy interest rate of the new policy cycle that began in June. We expect:

- The **European Central Bank** to trim its deposit facility rate by another quarter-point in December, with a quarterly cadence of quarter-point cuts next year, which would leave the policy rate at 3.25% at year-end 2024 and 2.25% at year-end 2025. The balance of risks skews toward even greater easing.
- Year-over-year headline **inflation** to remain around 2.20% and core inflation to fall to about 2.60% at year-end, before reaching the ECB's 2.00% target in 2025.
- The **unemployment rate** to end 2024 around current levels—it stood at a record-low 6.40% in July—though lower corporate profit margins skew risks to the upside.
- Full-year **economic growth** of only about 0.80%, as restrictive monetary and fiscal policy constrain activity.

United Kingdom

Although services inflation, pay growth, and GDP data have all recently undershot expectations, an 8-1 September 19 vote by central bank policymakers to maintain their 5.00% policy interest rate acknowledged that risks to resurgent inflation remained. We expect:

- The **Bank of England (BOE)** to cut the bank rate in November with the policy rate ending 2024 at 4.75% and quarterly with 0.25-percentage-point cuts in 2025. Even greater easing seems more likely than less easing.
- **Economic growth** to moderate in the second half of the year, leaving full-year growth of 1.20%.
- **Core inflation** to end 2024 around 2.80% year over year—it stood at 3.60% in August—and to hit the BOE's 2.00% target by the second half of 2025.
- The **unemployment rate** to end 2024 in a range of 4.00%–4.50%, with risks skewed to the upside. The rate stood at 4.10% in the May–July period.

China

Sluggish domestic demand highlights the risk that China's target of 5.00% economic growth this year may not be met. Increased government loan issuance in August provides hope, but more of the same will likely be required in the months ahead. We expect:

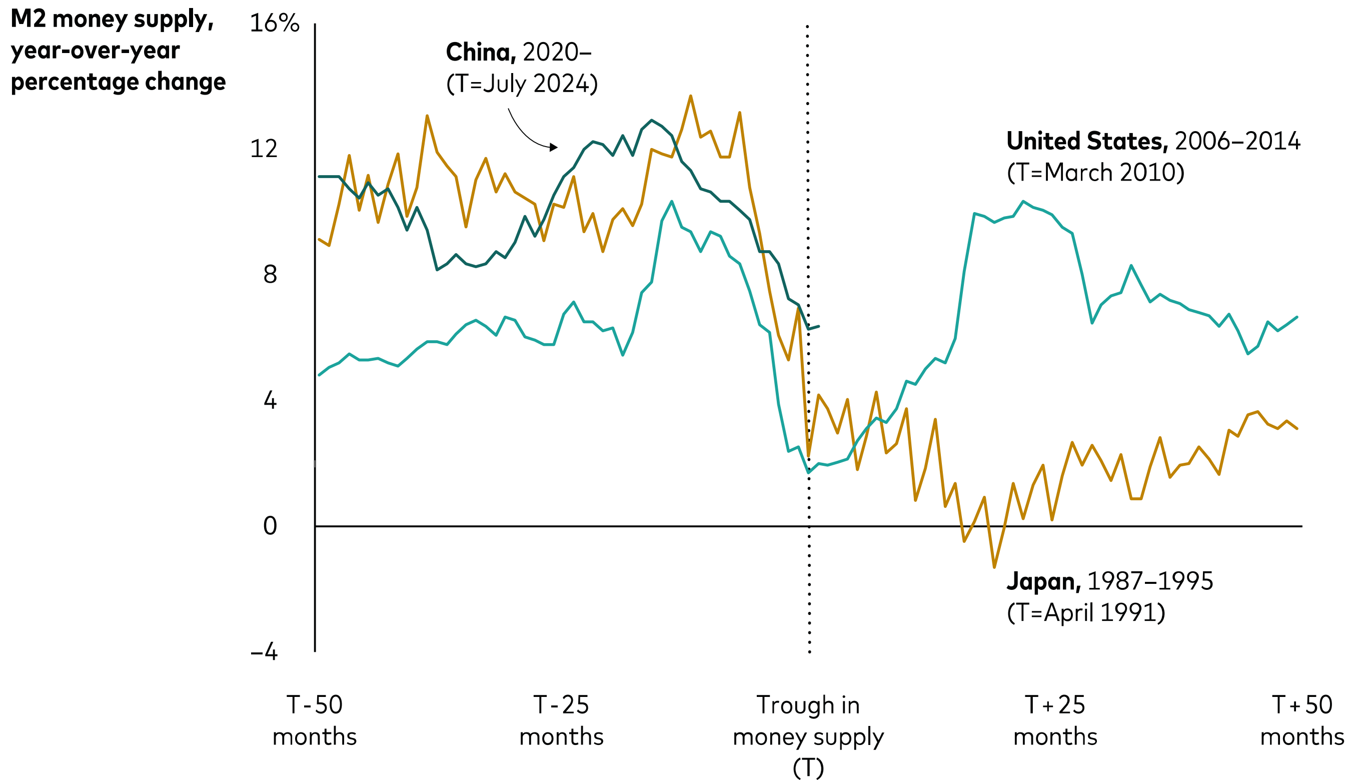
- A 0.10 percentage point cut this year in the seven-day reverse repo rate, the policy rate of the **People's Bank of China**. The policy rate stands at 1.70%. There may be further reductions in the banks' reserve requirement ratios as well.
- That China will still reach its **economic growth** target for 2024 provided that a sufficiently timely policy response occurs.
- Mild reflation this year, with headline **inflation** of 0.80%, and core inflation, which excludes food and energy prices, of 1.00%. Producer prices fell on a year-over-year basis for the 23rd consecutive month in August.

A recent rapid decline in its money supply highlights deflationary concerns in China. The GDP deflator, a broad, inflation-adjusted measure of economic output, has been negative for five consecutive quarters. Judging by recent experiences in the United States and Japan, China will be challenged in its efforts to lift barely positive consumer inflation closer to the People's Bank of China's 3.00% target.

Grappling with a property-driven slowdown, China has introduced several stimulative measures this year. Most have been aimed at the supply side.

"Policy aimed at stoking demand to boost confidence among China's consumers is likely required in addition to the supply-side measures," said Grant Feng, a Vanguard senior economist who studies the Asia-Pacific region. "People won't spend on goods and services if they expect that prices will be lower next month. That would mean further downward pressure on prices and a harder road back toward potential growth."

Lessons for China in experiences of the U.S. and Japan



Sources: Vanguard calculations, based on data from CEIC Data through July 31, 2024.

Notes: "T" represents a trough in M2 money in circulation. Increments before and after the troughs are in months. M2 is a broad measure of money in circulation that includes all aspects of M1 (such as physical currency and checking and savings accounts) plus other highly liquid assets such as certificates of deposit and money market accounts.

Our chart reflects a relatively swift return to previous M2 money-in-circulation levels in the United States following the global financial crisis, which was aided by timely consumer-focused stimulus. "A quick and decisive policy response is critical to fighting deflationary risk," said Qian Wang, Vanguard chief economist for the Asia-Pacific region. "The U.S. after the global financial crisis offers a good example of this, whereas Japan in the 1980s and 1990s lacked a swift and sufficient response. There is a good lesson for China in these experiences."

Emerging markets

Services inflation remains sticky in most emerging markets, but that hasn't stopped a cycle of interest rate cuts as broader inflation readings approach central bank targets. Since our economic survey last month, policy rates have been reduced by 0.25 percentage points in such markets as **Chile, the Philippines, the Czech Republic,** and **Mexico**.

A notable exception is **Brazil**, where the central bank raised its policy rate to 10.75% on September 18, reversing a cutting cycle that began in August 2023. Brazil's currency, the real, has depreciated by 13.00% against the U.S. dollar since the start of the year, through September 17.

In Mexico, we expect:

- Another 0.50–1.00 percentage point of **policy interest rate** cuts in 2024, to a year-end range of 9.75%–10.25%, levels that would still be restrictive.
- The rate of core **inflation** to finish 2024 near the upper end of Banxico's 2.00%–4.00% target range. It stood at 4.00% on a year-over-year basis in August.
- Full-year **economic growth** of 1.75%–2.25%. We'll be watching for signs of restrictive policy rates weighing on consumption and fixed asset investment.

All investing is subject to risk, including the possible loss of the money you invest.

Investments in bonds are subject to interest rate, credit, and inflation risk.

Investments in stocks and bonds issued by non-U.S. companies are subject to risks including country/regional risk and currency risk. These risks are especially high in emerging markets.

IMPORTANT: The projections and other information generated by the Vanguard Capital Markets Model (VCMM) regarding the likelihood of various investment outcomes are hypothetical in nature, do not reflect actual investment results, and are not guarantees of future results. VCMM results will vary with each use and over time.

The VCMM projections are based on a statistical analysis of historical data. Future returns may behave differently from the historical patterns captured in the VCMM. More important, the VCMM may be underestimating extreme negative scenarios unobserved in the historical period on which the model estimation is based.

The Vanguard Capital Markets Model® is a proprietary financial simulation tool developed and maintained by Vanguard's primary investment research and advice teams. The model forecasts distributions of future returns for a wide array of broad asset classes. Those asset classes include U.S. and international equity markets, several maturities of the U.S. Treasury and corporate fixed income markets, international fixed income markets, U.S. money markets, commodities, and certain alternative investment strategies. The theoretical and empirical foundation for the Vanguard Capital Markets Model is that the returns of various asset classes reflect the compensation investors require for bearing different types of systematic risk (beta). At the core of the model are estimates of the dynamic statistical relationship between risk factors and asset returns, obtained from statistical analysis based on available monthly financial and economic data from as early as 1960. Using a system of estimated equations, the model then applies a Monte Carlo simulation method to project the estimated interrelationships among risk factors and asset classes as well as uncertainty and randomness over time. The model generates a large set of simulated outcomes for each asset class over several time horizons. Forecasts are obtained by computing measures of central tendency in these simulations. Results produced by the tool will vary with each use and over time.

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The Value of Ownership

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